

County's purpose for relocating the Transmission Line is to accommodate the widening of a public highway. The relocation of the Transmission Line does not directly benefit particular customers or potential customers of Utility in their capacity as customers.

Parent represents the following under penalties of perjury: The relocation of the Transmission Line is not a prerequisite to the provision of any services. The relocated Transmission Line will not provide any additional or upgraded electric service beyond what it currently provides. The residents of any future development could become electric customers of Utility, but they will not be served by the Transmission Line.

Parent requests a ruling that the payments by County or another governmental subdivision acting as the agent of County to Utility for Project for the purpose of relocating the Transmission Line are not a contribution in aid of construction (CIAC) under section 118(b) and are a contribution to the capital of Utility under section 118(a).

LAW AND ANALYSIS

Section 61(a) and section 1.61-1 of the Income Tax Regulations provide that gross income means all income from whatever source derived, unless excluded by law. Section 118(a) provides that, in the case of a corporation, gross income does not include any contribution to the capital of the taxpayer. Section 118(b) provides that for section 118(a) purposes, the term "contribution to the capital of the taxpayer" does not include any CIAC or any other contribution as a customer or potential customer.

The House Ways and Means Committee Report for the Tax Reform Act of 1986 explains that property, including money, is a CIAC (rather than a capital contribution) if it is transferred to provide or encourage the provision of services to or for the benefit of the person transferring the property. H.R. Rep. No. 426, 99th Cong., 1st Sess. 644 (1985), 1986-3 (Vol. 2) C.B. 644 (the House Report). A utility has received property to encourage the provision of services if the receipt of the property is a prerequisite to the provision of the services; if the receipt of the property results in the provision of services earlier than would have been the case had the property not been received; or if the receipt of the property otherwise causes the transferor to be favored in any way. However, a transfer of property is not a CIAC where it is clearly shown that the benefit of the public as a whole was the primary motivating factor in the transfer.

Notice 87-82, 1987-2 C.B. 389, provides that a payment received by a utility is not a CIAC if it does not reasonably relate to the provision of services by the utility or for the benefit of the person making the payment, but rather relates to the benefit of the public at large. Notice 87-82 provides as an example of a payment benefiting the public at large a relocation payment received by a utility under a government program to place utility lines underground. In that situation, the relocation payment is not considered a CIAC where the relocation is undertaken for purposes of community aesthetics and public safety and does not directly benefit particular customers of the utility in their

capacity as customers. Notice 87-82 provides that similar principles apply where the utility is being reimbursed for the costs of relocating utility lines to accommodate the construction or expansion of a highway and not for the provision of utility services.

The payments by County to Utility for Project for the purpose of relocating the Transmission Line will benefit the public at large by widening a public highway. Therefore, we conclude that the payments by County to Utility for Project for the purpose of relocating the Transmission Line fall within the public benefit exception described in the House Report and in Notice 87-82 and are not a CIAC under section 118(b).

Next, we must decide whether the payments qualify as a contribution to capital under section 118(a).

The legislative history of section 118 provides, in part, as follows:

This [section 118] in effect places in the Code the court decisions on the subject. It deals with cases where a contribution is made to a corporation by a governmental unit, chamber of commerce, or other association of individuals having no proprietary interest in the corporation. In many such cases because the contributor expects to derive indirect benefits, the contribution cannot be called a gift; yet the anticipated future benefits may also be so intangible as to not warrant treating the contribution as a payment for future services.

S. Rep. No. 1622, 83rd Cong., 2d Sess. 18-19 (1954).

In Detroit Edison Co. v. Commissioner, 319 U.S. 98 (1943), the Court held that payments by prospective customers to an electric utility company to cover the cost of extending the utility=s facilities to their homes were part of the price of service rather than contributions to capital. The case concerned customers= payments to a utility company for the estimated cost of constructing service facilities (primary power lines) that the utility company otherwise was not obligated to provide. The customers intended no contribution to the company=s capital.

Later, in Brown Shoe Co. v. Commissioner, 339 U.S. 583 (1950), the Court held that money and property contributions by community groups to induce a shoe company to locate or expand its factory operations in the contributing communities were nonshareholder contributions to capital. The Court reasoned that when the motivation of the contributors is to benefit the community at large and the contributors do not anticipate any direct benefit from their contributions, the contributions are nonshareholder contributions to capital. Id. at 591.

Finally, in United States v. Chicago, Burlington & Quincy Railroad Co., 412 U.S. 401, 413 (1973), the Court, in determining whether a taxpayer was entitled to depreciate the cost of certain facilities that had been funded by the federal government, held that the governmental subsidies were not contributions to the taxpayer=s capital. The Court recognized that the holding in Detroit Edison Co. had been qualified by its decision in Brown Shoe Co. The Court in Chicago, Burlington & Quincy Railroad Co. found that the distinguishing characteristic between those two cases was the differing purpose motivating the respective transfers. In Brown Shoe Co., the only expectation of the contributors was that such contributions might prove advantageous to the community at large. Thus, in Brown Shoe Co., since the transfers were made with the purpose not of receiving direct services or recompense, but only of obtaining advantage for the general community, the result was a contribution to capital.

The Court in Chicago, Burlington & Quincy Railroad Co. also stated that there were other characteristics of a nonshareholder contribution to capital implicit in Detroit Edison Co. and Brown Shoe Co. From these two cases, the Court distilled some of the characteristics of a nonshareholder contribution to capital under both the 1939 and 1954 Codes. First, the payment must become a permanent part of the transferee=s working capital structure. Second, it may not be compensation, such as a direct payment for a specific, quantifiable service provided for the transferor by the transferee. Third, it must be bargained for. Fourth, the asset transferred foreseeably must benefit the transferee in an amount commensurate with its value. Fifth, the asset ordinarily, if not always, will be employed in or contribute to the production of additional income and its value assured in that respect.

The payments by County to Utility for Project for the purpose of relocating the Transmission Line contain the characteristics of a nonshareholder contribution to capital described in Chicago, Burlington & Quincy Railroad Co. Therefore, we conclude that the payments by County to Utility for Project for the purpose of relocating the Transmission Line are a contribution to the capital of Utility under section 118(a).

CONCLUSION

Accordingly, based on the foregoing analysis and the representations made, we conclude that the payments made by County or another governmental subdivision acting as the agent of County to Utility for Project for the purpose of relocating the Transmission Line and related equipment are not a CIAC under section 118(b) and are a contribution to the capital of Utility under section 118(a).

Except as specifically set forth above, no opinion is expressed or implied regarding the federal income tax consequences of the above described facts under any other provision of the Code or regulations.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this ruling request, a copy of this letter is being sent to Parent's authorized representative.

Sincerely,

NICOLE R. CIMINO
Senior Technician Reviewer, Branch 5
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2):
Copy of this letter
Copy for section 6110

cc: